

FINDING OF EMERGENCY

CALIFORNIA CODE OF REGULATIONS TITLE 14. NATURAL RESOURCES DIVISION 2. DEPARTMENT OF CONSERVATION CHAPTER 5. DIVISION OF RECYCLING

FINDING OF EMERGENCY

The Department of Resources Recycling and Recovery (CalRecycle/Department) is proposing emergency regulations to amend section 2975, Subchapter 12, Chapter 5, Division 2, Title 14, of the California Code of Regulations (CCR) that lays out the reasonable financial return calculation for processing payments. This change will help support beverage container recycling in California by establishing, for calendar year 2018, a reasonable financial return that takes into account rural business circumstances and factors such as known cost increases. This will provide for increases in convenience by increasing the profitability of recycling centers.

The adoption of these regulations is deemed to be an emergency pursuant to Public Resources Code Sections 14536.1 which provides that “if the department determines that it is necessary to adopt or amend regulations to implement Section 14575, the department may adopt or amend those regulations as emergency regulations. The Office of Administrative Law shall consider those regulations to be necessary for the immediate preservation of the public peace, health and safety, and general welfare for purposes of Section 11349.6 of the Government Code. Notwithstanding subdivision (e) of Section 11346.1 of the Government Code, the emergency regulations adopted or amended pursuant to this section shall be repealed 180 days after the effective date of the regulations, unless the department complies with Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code.”

FINDING OF NECESSITY

The California Beverage Container Recycling Program (BCRP) was established as a California Redemption Value (CRV) deposit and return system to create convenient beverage container recycling opportunities in the state. Recycling centers that redeem CRV containers located throughout the state provide opportunities for consumers to return their CRV beverage containers to claim their deposit. The Department works to create and maintain a marketplace that provides consumers with convenient recycling opportunities. Tools the department uses include education and supplemental payments that include processing payments. Processing payments reimburse recyclers for the difference between the cost of recycling a pound of beverage container material and the value a recycler receives when it sells that material as scrap.

When the BCRP was created thirty years ago, the law provided for a “reasonable financial return” for recycling centers in order to insure the economic recovery of the beverage containers. This “reasonable financial return” was further clarified in the CCR section 2975 which states that “The statewide average reasonable financial return for recycling centers shall be equal to the statewide average allowable costs calculated in section 2960 of this subchapter, multiplied by the average return on costs for the scrap and waste materials industry as determined from data contained in the most recent Dun and Bradstreet Standard Three Year Norm Report (Published by Dun and Bradstreet Credit Services).” Due to adverse market conditions, the average return on costs reported by Dun and Bradstreet resulted in a negative reasonable financial return for the first time in 2017.

This emergency rulemaking will, for calendar year 2018, provide a higher processing payment by setting the reasonable financial return for calendar year 2018 at 11.5 percent for all recyclers except that a reasonable financial return of 16.6 percent would be applied to rural region recycling centers. The department intends to revisit these issues as part of a permanent rulemaking process during 2018. The term “recycler” for purposes of this rulemaking has the same definition as in PRC §14519.5., i.e., “recycler”

means a recycling center, dropoff or collection program, or curbside program. All of these entities receive processing payments.

The Department proposes to amend or add the following sections to the California Code of Regulations, Title 14, Division 2, Chapter 5, Subchapter 12, Article 2:

Section 2975 will be amended to designate this as subsection (a) in order to add a new subsection (b).

Section 2975(b) adds a new subsection to establish a specified reasonable financial return for a limited time effective from January 1, 2018, to December 31, 2018.

Section 2975(b)(1) adds a new paragraph to authorize a reasonable financial return that is equal to eleven and five-tenths percent of the statewide allowable costs in section 2960. Section 2960 provides the categories of recycling center costs used for calculating processing payments. The eleven and five-tenths percent value reflects, in part, the impacts of minimum wage increases on recycling center costs. Further, in response to feedback from industry that the RFR needs to be increased, the department has selected these percentages in an attempt to balance the profitability of recycling centers and financial impact on the Fund. A more detailed description of how the percentages were calculated can be found in the Informative Digest, below.

Section 2975(b)(1)(A) adds a new clause that authorizes a reasonable financial return of sixteen and six-tenths percent for rural region recycling centers to address a lack of convenience and higher operating costs in rural regions.

AUTHORITY

These regulations are submitted pursuant to the Department's authority under Public Resources Code subsections (PRC) 14530.5(b), 14536, and 14536.1.

REFERENCE

Title 14 CCR amended Section 2975 is intended to implement, interpret and make specific PRC 14501(f) and (g), 14518.5, and 14575.

INFORMATIVE DIGEST

The California Beverage Container Recycling and Litter Reduction Act, AB 2020/Margolin, Chapter 1290, Statutes of 1986 (Act), created the BCRP and established the Division of Recycling to administer the BCRP. The intent of the BCRP is to provide increased and convenient beverage container redemption and recycling opportunities for consumers. These changes will provide for further increases in convenience by increasing the profitability of recycling centers. This is accomplished through the establishment of the CRV for eligible beverage containers and working with industry participants such as recyclers and processors who are certified by the Department.

Section 14501 (f) of the Act establishes the purpose of the BCRP, including to create and maintain a marketplace where it is profitable to establish sufficient recycling centers and locations to provide consumers with convenient recycling opportunities. The responsibility to provide convenient, efficient, and economical redemptions opportunities rests jointly with manufacturers, distributors, dealers, recyclers, processors, and the Department (Section 14501(g)). Section 14518.5 defines the term “processing payment.” Section 14575 establishes the processing fee, paid by beverage manufacturers and offset by the Beverage Container Recycling Fund (Fund), and the processing payment, paid to recyclers.

CalRecycle annually establishes the reasonable financial return (RFR) each January, which is applied to the calculation of the processing payment. The rates are determined consistent with the Act and a long-standing, defined regulatory calculation. The source used to determine the RFR, as specified in regulation, is the most recent average net profit ratio of businesses classified as scrap and waste materials as reported by Dun and Bradstreet. For the first time since the BCRP began using the Dun and Bradstreet indicator in 2001, the RFR was a negative value: for 2017, the RFR was calculated to

be -5.85 percent of allowable costs, a reflection of the overall losses, rather than profits, of the recycling industry. This resulted in lower processing payments to certified entities than the amount necessary to cover the cost of recycling. At the same time, low prices for scrap material, along with other factors such as difficulty in finding locations willing to host recycling centers, led some recycling centers to close, leaving communities with fewer places for people to redeem CRV containers. To provide more support to the recycling industry than what would be provided under the current regulations, CalRecycle is proposing to implement an 11.5 percent RFR for non-rural recyclers and a 16.6 percent RFR for rural region recycling centers when calculating processing payments for 2018. An additional RFR is assigned to rural recycling centers based on operating costs for recycling centers in rural areas being higher. These percentages reflect, in part, recent and expected state minimum wage increases that would otherwise not be captured until the department's next periodic survey of recycling center costs. Further, in response to feedback from industry that the RFR needs to be increased, the department has selected these percentages in an attempt to balance the profitability of recycling centers against financial impacts to the Fund.

What follows is a description of the methodology used to arrive at the percentages reflected in this rulemaking.

A base of 5% RFR for urban recycling centers was calculated as the lowest RFR that could be given while still keeping processing payments at approximately the same level for 2018 as they were in FY 2016-17 and ensuring a reasonable financial return. CalRecycle anticipated lower processing payments in 2018 based on a prior decrease of 7% in PET cost per ton from 2012 to 2014 as published in the 2015 Cost Survey. Additionally, in the year 2017, CalRecycle heard from consumers and received considerable media coverage on consumers inability to recycle due recent recycling center closures (partly caused by low processing payments). Correspondingly, CalRecycle saw the recycling rate drop below 80% for the first time in many years. To address the decline in recycling infrastructure and loss of convenient recycling options, CalRecycle sought to set

an RFR that would encourage recycling centers to stay in business and that would assure them at least the same processing payments as the prior year and provide stability to a market that has become increasingly volatile in recent months.

The dollar amount of processing payments for FY 2016-17 was taken and used as the base for calculating 2018 processing payments. The scrap prices were kept the same, but 2017 lower cost per ton estimations were used to calculate the difference between scrap prices and the cost of handling material to determine the amount of processing payment needed for a recycling center to break even. Due to lower cost estimations, processing payments for 2018 were cut by \$10 million. The RFR was then increased incrementally from -5.85% (2017 RFR) to 5% (proposed RFR) until the amount of processing payments was equal to FY 2016-17, which resulted in an increase of 10.85% RFR and resulting in an overall 5% RFR ($-5.85 + 10.85 = 5$).

The additional 5% RFR given to rural recycling centers was based on an observed cost differential for urban and rural recycling centers recycling one ton of PET as measured by the CalRecycle 2014 Cost Survey. The 2014 average cost of recycling PET (the most prevalent material recycled) was \$410/ton for urban recycling centers and \$715/ton for rural recycling centers. (The department chose to make the rural RFR double that of non-rural). CalRecycle determined that because operating costs were higher for rural centers compared to urban centers, a higher RFR was needed to help ensure fiscal feasibility of rural recycling center operations for provide redemption opportunities that otherwise may not have existed.

A minimum wage adjustment of 1.4% and 1.5% was added to the base 5%/10% proposed RFR to bring the proposed RFR to 6.4% (urban) and 11.5% (rural) (see below). After proposing a 6.4%/11.5% RFR at a public meeting, stakeholders requested an alternate proposal of 11.5%/16.6% citing additional needed financial support. In the spirit of collaborative policy-making and in an attempt to

address stakeholder needs, the Department agreed to put forth a proposal for a 2018 RFR of 11.5%/16.6% for the period of one year until more permanent solutions can be made.

Between 1988 and 2016, minimum wage increases occurred with relative infrequency, averaging about 33 months between each increase. Beginning on January 1, 2016, minimum wage increases have been scheduled every 12 months, with the last currently scheduled increase occurring January 1, 2023. Due to the logistics of gathering data, the cost of recycling, measured via a survey conducted by the department every two years, is applied to the processing payment calculation either two or three years after the year that the costs are measured. With annual increases in the minimum wage, the measured cost of recycling is not keeping current with increases in labor costs. A broad inflation adjustment is applied annually to the measured cost of recycling. To improve the accuracy of the cost of recycling applied to the processing payment, the department will incorporate a minimum wage adjustment in the setting of the RFRs to more timely reflect the annual increases in the minimum wage.

The following methodology was used to calculate the minimum wage portion of the RFR:

The general formula for the minimum wage adjustment is $(\% \text{ increase in minimum wage}) \times (\text{proportion of allowable costs labor}) \times (\text{proportion of payroll impacted})$

The percent increase in minimum wage equals the minimum wage in effect for the year the rate is calculated divided by the minimum wage in effect during the year costs were measured.

The proportion of allowable costs for labor is intended to isolate only the type of costs that are directly impacted by a change in minimum wage; for example, there is little expectation that costs such as rent, utilities, or supplies would be directly impacted by an increase in labor costs, and any such change in other costs is intended to be reflected by the COLA.

The proportion of payroll impacted is the proportion of all labor hours that were paid at or below minimum wage reflecting that not all employee wages will automatically increase.

The proportion of allowable costs labor and proportion payroll directly impacted are provided from the cost survey.

The table below details the calculation of the minimum wage adjustment based on costs measured in 2016 to be applied to processing payments in effect for 2018 (2017 is shown for continuity):

Year	Minimum Wage (\$/hr.)	% Increase in Minimum Wage	Proportion Allowable Costs Labor (1)	Proportion of Payroll Impacted	Minimum Wage Adjustment
2016	\$10.00				
2017	\$10.50	5.0%	59.2%	23.0%	0.68%
2018	\$11.00	10.0%	59.2%	23.0%	1.36%

(1) Based on 2014 measured costs; the 2016 proportions are not yet

The Department finds that an emergency exists to amend existing regulations in order to implement statutory mandates of PRC section 14575. The proposed regulations would amend section 2975 of the CCR Title 14. Natural Resources, Division 2. Department of Conservation, Chapter 5. Division of Recycling, Subchapter 12, Article 2. The adoption of these regulations is deemed to be an emergency pursuant to PRC section 14536.1 which provides that “if the department determines that it is necessary to adopt or amend regulations to implement Section 14575, the department may adopt or amend those regulations as emergency regulations. The Office of Administrative Law shall consider those regulations to be necessary for the immediate preservation of the public peace, health and safety, and general welfare for purposes of Section 11349.6 of the Government Code. Notwithstanding subdivision (e) of Section 11346.1 of the Government Code, the emergency regulations adopted or amended pursuant to this section shall be repealed 180 days after the effective date of the regulations, unless the department complies with Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code”).

There are no federal regulations or statutes comparable to these proposed regulations. The proposed regulations are not inconsistent or incompatible with existing state regulations. The BCRP is unique to the state of California and there is not a similar program within the state. There are no other matters prescribed by statute applicable to this specific state agency or to any specific regulation or class of regulations.

SPECIFIC AGENCY STATUTORY REQUIREMENTS

There are no specific agency statutory requirements relevant to this rulemaking.

LOCAL MANDATE DETERMINATION

The proposed regulations do not impose a mandate on local agencies or school districts.

FISCAL IMPACT ESTIMATE

This change will result in approximately \$12.6 million additional expenditure for processing payments to be funded by a \$2.5 million increase in processing fee revenue paid by beverage manufacturers and an additional \$10.8 million in transfers from the Fund to the Processing Fee accounts as prescribed in PRC section 14575.

The proposed emergency regulations will not result in either costs or savings to any other State Agency, local agencies or school districts. Approximately 4 percent of processing payment recipients are local government entities who run recycling programs. The total amount of approximately \$510,000 distributed to these entities over the course of these emergency regulations will not have a significant impact. Further, these proposed emergency regulations will not result in any non-discretionary cost or savings to any local agencies, nor will they result in cost or savings to federal funding to the State.

DOCUMENTS RELIED UPON

The Department utilizes two sources from the California Department of Industrial Relations for the minimum wage costs:

Present and future: https://www.dir.ca.gov/dlse/faq_minimumwage.htm

Historical: <https://www.dir.ca.gov/iwc/minimumwagehistory.htm>

NOTICE OF REGULATORY ACTION

The Department has complied with the requirement to provide notice of the proposed emergency rulemaking pursuant to Government Code Section 11346.1(a) (2).

Government Code section 11346.1(a) (2) requires that, at least five working days prior to submission of the proposed emergency action to the Office of Administrative Law, the adopting agency provide a notice of the proposed emergency action to every person who has filed a request for notice of regulatory action with the agency. After submission of the proposed emergency to the Office of Administrative Law, the Office of Administrative Law shall allow interested persons five calendar days to submit comments on the proposed emergency regulations as set forth in Government Code section 11349.6.

A copy of the memorandum transmitting the proposed emergency text and the proposed Statement of Emergency to interested parties is included in the emergency rulemaking file.